7-1-1964

Creditors' Rights

Warren M. Solomon

CREDITORS' RIGHTS*

WARREN N. SALOMON**

INTRODUCTION

This is the first survey of creditors' rights in Florida, the major emphasis of which is on non-bankruptcy devices. In the main, bankruptcy cases have been included only when the rights of the trustee in bankruptcy conflicted with those of a secured creditor. Many of the cases contained herein make no significant changes in the law, yet they have been included to present a more comprehensive picture.

I. NON-BANKRUPTCY CREDITORS' REMEDIES

A. *Enforcement of Judgment*

1. EXECUTION

In proceedings supplementary to execution, the requirement of due process was read into section 55.57 of the Florida Statutes to the effect that property which the judgment debtor and his wife owned by the entireties was held not subject to levy pursuant to a judgment against the husband alone. Such proceedings cannot determine the property rights of a person not a party thereto.[1]

---

* This survey includes cases reported in 139 So.2d through 160 So.2d, and in 300 F.2d through 327 F.2d, No. 3.

** Member of Florida Bar; Editorial Board, *University of Miami Law Review.*

1. Crawford v. United States Fid. & Guar. Co., 139 So.2d 500 (Fla. 1st. Dist. 1962).

2. ATTACHMENT

It has been held that attachment is not available when there is no cause of action against the owner of the property.[2] In that case, the plaintiff, whose property had been confiscated by Cuba, tried to attach assets of the defendant, a Florida corporation, alleging that those assets were Cuban property. The writ of attachment was dissolved when the plaintiff failed to establish that the defendant itself was indebted to him. Since he had no basis for a suit against the defendant, he could not attach its assets.

The supreme court resolved a conflict between sections 76.07 and 76.11 of the Florida Statutes, which set out the required allegations in an affidavit for a writ of attachment. The former section requires the petitioner to state that he *believes* in the existence of the necessary grounds for the writ, while the latter section is satisfied by merely stating that the petitioner has good reason to believe in the existence of the statutory grounds. The court decided that the more stringent requirements of section 76.07 must be followed, despite the fact that the petitioner used printed forms of the affidavit, furnished by the Clerk of the Circuit Court, which contained the less stringent language of section 76.11.[3]

In an action for wrongful attachment, which is similar in nature to an action for malicious prosecution, it was held that the plaintiff's lost profits were not a proper item to be recovered. Damages are limited to the "use value" of the property attached, plus the loss or injury caused the plaintiff by the attachment.[4]

3. GARNISHMENT

Recent cases illustrated several defenses to the writ of garnishment. Garnishment proceedings were brought against a surety by a judgment creditor of the principal. As a defense, the garnishee-surety alleged that no debt was owed to the principal, and the writ was dissolved. The proper remedy of the judgment creditor would have been an action against the surety directly. Garnishment was improper because there was no debt owed by the surety to the principal.[5]

When the judgment creditor in an automobile collision case brought garnishment proceedings against the judgment debtor's insuror, the garnishee-insurance company claimed that the judgment debtor had failed

2. Cuba Aeropostal Agency, Inc. v. Kane, 145 So.2d 764 (Fla. 3d Dist. 1962).

3. General Finance Loan Co. v. Williams, 150 So.2d 440 (Fla. 1963).

4. Florida Transp. Co. v. Dixie Sightseeing Tours, Inc., 139 So.2d 175, 177 (Fla. 3d Dist. 1962).

5. Seaboard Surety Co. v. Acme Wellpoint Corp., 156 So.2d 688 (Fla. 2d Dist. 1963).

to cooperate with it in defending the suit. The defense would have been sufficient, had the alleged lack of cooperation been disclosed by the facts.[6]

In a rather confusing case, a bank issued a cashier's check and was then served with a writ of garnishment on that account. Subsequently, the bank paid the check to the drawer's attorney, believing him to be a holder in due course. The garnishing creditor never got his hands on the money and the garnishee-bank was held not liable to him. Apparently, a bank's first duty is to holders in due course, rather than to garnishing creditors.[7]

In *Smith v. Kirkland*,[8] the garnishee-insurance company had paid the judgment creditor to the full extent of its coverage of the judgment debtor. After receiving this payment, the judgment creditor failed to issue out a writ of scire facias as required by Rule 2.12(b) of the Florida Rules of Civil Procedure. Instead, the judgment creditor obtained a judgment against the garnishee-insurance company for the amount that had already been paid. It was held that the judgment so obtained was void for failure to issue out the required writ of scire facias. The writ of garnishment was dissolved, and the judgment against the garnishee was expunged from the court's records.

Since the purpose of the writ of scire facias is to give notice to the garnishee against whom execution is about to be issued, so that he can raise new defenses that have arisen *after* the writ of garnishment has been served, defenses that would have been available against the writ of garnishment (like "no debt") cannot be raised in response to scire facias.[9]

Section 77.26 of the Florida Statutes provides that when a writ of garnishment is dismissed, the defendant in garnishment is entitled to attorney's fees as costs. Such fees must be determined upon a hearing, as must any other controverted issue, and not merely by the use of an affidavit.[10]

Florida recognizes a tort action for the wrongful and malicious seizure of property under a writ of garnishment. A complaint was held to state a cause of action when the garnishing creditor knew that the judgment debtor was the head of a family residing in Florida, whose wages could not be garnished,[11] yet alleged the opposite in the garnishment affidavit.[12]

6. State Farm Mutual Auto. Ins. Co. v. Ware, 159 So.2d 262 (Fla. 3d Dist. 1964).

7. Universal C.I.T. Credit Corp. v. Broward Nat'l Bank, 144 So.2d 844 (Fla. 2d Dist. 1962).

8. 155 So.2d 553 (Fla. 3d Dist. 1963).

9. Seven-Up Bottling Co. v. J. N. Rawleigh Co., 156 So.2d 180 (Fla. 2d Dist. 1963).

10. Beasley v. Wolf, 151 So.2d 679 (Fla. 3d Dist. 1963).

11. FLA. STAT. § 222.11 (1963).

12. Strickland v. Commerce Loan Co., 158 So.2d 814 (Fla. 1st. Dist. 1963).

4. SUPPLEMENTARY PROCEEDINGS[13]

Rights of third parties cannot be adjudicated in proceedings supplementary to execution unless they have been afforded due process. The wife of a judgment debtor could not be ordered to turn over 10,000 dollars to her husband's judgment creditor when she was not a party to the original action and had never been served.[14]

5. CREDITORS' BILL[15]

A creditors' bill is a proceeding in equity brought by a creditor for the purpose of reaching property of the debtor which cannot be reached by ordinary legal process. The usefulness of this device was pointed out in *Money v. Powell*,[16] when the defendant in a tort action conveyed his undivided interest in realty to his wife a few days after the accident. After the tort action was filed, the plaintiff elected to have the fraudulent conveyance set aside by means of a creditors' suit, rather than wait until judgment to levy on the property. It was unnecessary to join in the action the other undivided owners of the realty.

6. EXEMPTIONS

Article X, section 1 of the Florida Constitution, relating to homestead, was construed to exempt from forced sale not only a dwelling house, but also an adjacent pool, garage, and apartment over the garage. The court stated that constitutional and statutory provisions relating to homestead should be liberally construed.[17] The only explicit limitation which the constitution places on homestead is that the exempt area may not constitute more than one-half acre within the limits of a city or town.

The doctrine of sovereign immunity will protect the chattels of a foreign government from judicial sale. In a case in which that defense was not timely raised, however, the doctrine was held not to extend to the *proceeds of* a judicial sale. The court pointed out that after the sale it no longer had control over the chattels (3 Cuban airplanes), and the proceeds of the sale had become the property of the judgment creditor.[18]

Section 222.13 of the Florida Statutes, which declares that life insurance proceeds "shall be exempt from the claims of creditors of the insured," was held to be not only an exemption statute, but also to create a rule of law with respect to the descent and distribution of property.[19]

13. FLA. STAT. §§ 55.52-.611 (1963).
14. Tomayko v. Thomas, 143 So.2d 227 (Fla. 3d. Dist. 1962).
15. FLA. STAT. § 62.37 (1963).
16. 139 So.2d 702 (Fla. 2d Dist. 1962).
17. White v. Posick, 150 So.2d 263 (Fla. 2d Dist. 1963).
18. United States v. Harris & Co. Advertising, Inc., 149 So.2d 384 (Fla. 3d Dist. 1963). Strangely enough, it was the United States that intervened on behalf of the Cuban government.
19. *In re* Alworth's Estate, 151 So.2d 478 (Fla. 1st Dist. 1963).

B. *Fraudulent Conveyances*

1. BULK SALES ACT[20]

The Bulk Sales Act provides that the sale of all or any portion of a stock of merchandise other than in the usual course of trade shall be presumed to be fraudulent as to the creditors of the vendor, unless there is compliance with the terms of the statute. The purpose of the Act is to prevent a sale of goods in bulk until the creditors of the vendor are paid in full.

Whether or not the presumption of fraud that arises when conveyances are made contrary to the Bulk Sales Act is rebuttable is an open question, which one recent case came close to resolving. However, the consideration for the conveyance, alleged to have been inadequate, failed because of the Statute of Frauds. Therefore, the conveyance was set aside without the necessity of looking into the adequacy of the consideration.[21]

2. CONDITIONAL SALES

Conditional sales contracts in which the vendee has possession of the goods, are deemed fraudulent only if they are unrecorded for longer than two years, in which case "absolute property shall be with the possession . . . ."[22] Vendors' liens on automobiles, however, must be recorded.[23] As a result, conditional vendors usually prevail in contests with subsequent lienors who claim that the conditional sale was fraudulent, because in a contest between two valid liens, the first in time is the first in right.[24]

A minority rule to the effect that the conditional vendor gives the conditional vendee *implied authority* to have repairs made was recently rejected in Florida, to the dismay of the mechanic's lienor who made repairs on a tractor and claimed that his right of possession was superior to that of the tractor's conditional vendor.[25]

An unrecorded conditional sales contract for a piano triumphed over a subsequent warehouseman's lien for storage,[26] in spite of the fact that except for Florida,[27] all states that have adopted the Uniform Ware-

---

20. FLA. STAT. ch. 726 (1963).

21. Cameron v. Federal Auto Parts, Inc., 301 F.2d 867 (5th Cir. 1962).

22. FLA. STAT. § 726.09 (1963).

23. FLA. STAT. § 319.15 (1963).

24. See text accompanying note 36 *infra*.

25. Richardson Tractor Co. v. Square Deal Mach. & Supply Co., 149 So.2d 388 (Fla. 2d. Dist. 1963).

26. Dade Nat'l Bank v. University Transfer & Storage, Inc., 151 So.2d 868 (Fla. 3d Dist. 1963).

27. FLA. STAT. ch. 678 (1963).

house Receipts Act which regards warehousemen's liens superior to liens derived by unrecorded conditional sales. This decision resulted from the fact that, as previously mentioned, Florida does not require that the conditional sales contract be recorded.[28]

However, not all conditional vendors have prevailed when goods were conditionally sold to a sub-lessee. In one case, the court pierced the vendor's corporate veil to find that the conditional vendor was the alter ego of the lessee; and on default of the sub-lessee, the title vested in the lessee, thereby subjecting the goods to the landlord's lien for rent.[29]

3. PROHIBITED TRANSFERS

Section 608.55 of the Florida Statutes forbids corporations from making conveyances for less than full credit to its stockholders, directors or officers, while the corporation is insolvent or while insolvency is imminent; or from giving one creditor a preference over others. Thus, where an insolvent corporation sold property to a director at a bargain price, as a "bonus," the sale was set aside.[30] Also, one case required the return by shareholders of dividends paid by a corporation while a judgment against it was being appealed, since the payment of the dividend, among other things, "depleted and denuded the judgment debtor to hinder, delay and defraud . . . judgment creditors."[31]

A federal court held that section 608.55 was limited to domestic corporations.[32] That case refused to set aside a transaction when an insolvent Bahamian corporation, doing business in Florida, gave preferential treatment to one of its officers by repaying his loan to the corporation at the expense of the corporation's other creditors.

C. *General Assignments*

The general assignment for the benefit of creditors is a little-used device; only one case in the last two years dealt with it. There, the property conveyed by the debtor to a trustee was subject to a mortgage, a fact which the debtor had not disclosed to the trustee. When the mortgagee tried to assert his claim against the trustee, the trustee defended on the ground that his title was that of a bona fide purchaser, and that therefore, the mortgage was invalid against him. It was held, however, that the trustee acquired the same title that the debtor-grantor had, and therefore the mortgagee prevailed.[33]

28. FLA. STAT. § 726.09 (1963).
29. Hyde of Massachusetts, Inc. v. Gray, 150 So.2d 267 (Fla. 3d Dist. 1963).
30. Garnett v. General Contractors & Builders, Inc., 145 So.2d 295 (Fla. 1st Dist. 1962).
31. Livesay Industries, Inc. v. Livesay Window Co., 305 F.2d 934, 940 (5th Cir. 1962).
32. Crane Co. v. Richardson Constr. Co., 312 F.2d 269 (5th Cir. 1963).
33. Kitchens v. Kitchens, 142 So.2d 343 (Fla. 2d Dist. 1962).

D. *Liens Generally*

1. NOTICE OF LIEN

In a case of first impression concerning the one-year limitation on the effectiveness of a notice of lis pendens,[34] it was decided that since the purpose of the statute is to prevent property from being tied up for an unreasonable period, the notice of lis pendens should be discharged after a year, especially when the lienor's claim against the property had previously been waived.[35]

2. CONTESTS BETWEEN LIENORS

Florida follows the rule of *United States v. City of New Britain*,[36] which holds that as between two perfected liens, the first in time is the first in right. Applying this rule, it was held that a lien for attorney's fees was subordinated to a federal tax lien, because at the time the tax lien was filed the amount of the attorney's fees (in a mortgage foreclosure suit) was uncertain.[37] In other words, the first perfected "choate" lien prevails.

Section 84.03(1) of the Mechanics' Lien Law formerly provided that "all liens provided by this Chapter shall relate to and take effect from the time of the visible commencement of operations . . . ." A mechanic's lienor tried to achieve a position of priority over a prior recorded mortgage by means of this "relation back" doctrine.[38] He failed, however, because he did not convincingly establish the existence of his lien prior to the recording of the mortgage.

In a contest between the conditional vendor of an automobile in Massachusetts, where recording of the contract was unnecessary, and a good faith purchaser of the automobile in Florida, who searched for and found no recorded liens, the Florida supreme court followed the rules of comity and gave effect to the Massachusetts conditional vendor's lien, stating that the Florida purchaser should have been more careful.[39]

3. PROPERTY SUBJECT TO LIENS

A liquor license may be the subject of a chattel mortgage and of a landlord's lien for rent. Even though the license is a privilege, it has the quality of property.[40]

---

34. FLA. STAT. § 47.49(2) (1963).

35. Marchand v. DeSoto Mortgage Co., 149 So.2d 357 (Fla. 2d Dist. 1963).

36. 347 U.S. 81 (1954).

37. United States v. First Fed. Sav. & Loan Ass'n, 155 So.2d 192 (Fla. 2d Dist. 1963).

38. Leedy v. First Fed. Sav. & Loan Ass'n, 142 So.2d 99 (Fla. 2d Dist. 1962). The Mechanics' Lien Law has since undergone major changes.

39. Municipal Auto Sales, Inc. v. Ferry Street Motor Sales, Inc., 143 So.2d 323 (Fla. 1962). See note, 17 U. MIAMI L. REV. 241 (1962).

40. Yarbrough v. Villeneuve, 160 So.2d 747 (Fla. 1st. Dist. 1964).

A case of first impression in Florida[41] held that the installation of wall-to-wall carpeting was not an improvement of real property within the meaning of the Mechanics' Lien Law.[42] The test used was: Has the article furnished become a part of the realty so as to be a fixture?

II. BANKRUPTCY

A. *Insolvency*

A debtor was found insolvent in spite of his claim that his assets were sufficient to enable him to pay his obligations within a reasonable period of time, because two of his assets were found to be without value: 1) an oral lease, which in Florida is a mere tenancy at will and without value in determining solvency; and 2) goodwill, which is an asset only with respect to an operating business, and valueless in this case because the debtor's business had ceased to function.[43]

B. *Contests Between Trustee and Secured Creditors*

An assignment of accounts receivable was made less than four months prior to the filing of an involuntary petition, and the trustee in bankruptcy sought to recover the funds collected by the assignee. The case hinged on whether or not the assignment had been perfected, which in turn hinged upon a construction of section 524.02 of the Florida Statutes, which provides that the assignee may perfect the assignment by filing a notice with the secretary of state. Instead of doing this, the assignee had given the individual debtors actual notice of the assignment. It was held that the statutory method of perfecting the assignment was *exclusive* of all other methods, and therefore the trustee's lien on the funds was prior to the unperfected claim of the assignee.[44]

In a later case, even though the assignee of accounts receivable filed the required notice, the assignment was set aside by the trustee as a mere voidable preference. The reason: The assignee was not considered a secured creditor because the assignment to it of the accounts receivable was not made to secure loans that it had made to the assignor, but instead, to secure loans *made by others* that had been assigned to the assignee. Thus, chapter 524 of the Florida Statutes is limited, protecting only those loans made *directly* by the assignee to the assignor of accounts receivable.[45]

In a contest between a trustee in bankruptcy and a field warehouseman, the warehouseman, in order to establish his lien, had the

41. Fell v. Messeroff, 145 So.2d 238 (Fla. 3d Dist. 1962).
42. FLA. STAT. ch. 84 (1963).
43. Mossler Acceptance Co. v. Martin, 322 F.2d 183 (5th Cir. 1963).
44. Miami Nat'l Bank v. Knudsen, 300 F.2d 289 (5th Cir. 1962).
45. James Talcott, Inc. v. Wilcox, 308 F.2d 546 (5th Cir. 1962).

burden of proving that the goods in question had been deposited with it. It was held that the mere fact that the goods were in the premises leased by the warehouseman was insufficient to establish the deposit of the goods according to section 678 of the Florida Statutes, and consequently, the lien of the trustee prevailed.[46]

The Uniform Limited Partnership Law provides that if a limited partner receives security for a loan while the partnership is insolvent, it is a fraud on the partnership's creditors.[47] Thus, it was held that when a partnership was solvent at the time it gave a mortgage to a limited partner as security for a loan, there was no fraud, and the mortgage was valid against the trustee in bankruptcy.[48]

A debtor paid off a note to a bank, and within four months was adjudicated bankrupt. The trustee tried to have the payment set aside as a voidable preference under section 68a of the Bankruptcy Act. It was held that since the bank was in no better position than if it had exercised its right of set-off, the payment would not be set aside.[49] In a later case, however, a creditor bank was held to have waived its right of set-off when it continued to accept monthly installments on its loan after the petition was filed. After the funds on deposit at the time of the petition were paid out, all funds deposited wtih the bank had to be turned over to the trustee in bankruptcy for the benefit of all unsecured creditors.[50]

III. CORPORATE REORGANIZATION

A. *Parties*

Secured creditors attempted to have their debtor's voluntary petition for a Chapter X reorganization set aside by claiming that since the debtor was a corporation owned by a single stockholder who controlled other interlocking corporations, it could not properly qualify as a "corporation."[51] The petition was not set aside, because there was no evidence that the corporate structure was a fraud on creditors, and the petitioner was held to qualify as a corporation within the definition of 11 U.S.C., section 1(8).

B. *Requirement of Good Faith*

The mere fact that a class of secured creditors has announced that it will not consent to any plan of re-organization does not make it impossible for the debtor to file a petition for reorganization in good faith,

46. Lawrence Warehouse Co. v. McKee, 301 F.2d 4 (5th Cir. 1962).
47. FLA. STAT. § 620.13(2) (1963).
48. Hughes v. Dash, 309 F.2d 1 (5th Cir. 1962).
49. McKee v. Hood, 312 F.2d 394 (5th Cir. 1963).
50. First Nat'l Bank v. Davis, 317 F.2d 770 (5th Cir. 1963).
51. Corr v. Flora Sun Corp., 317 F.2d 708 (5th Cir. 1963).

in spite of section 146(3) of the Bankruptcy Act, which provides that a petition shall be deemed "not to be filed in good faith if . . . it is unreasonable to expect that a plan of reorganization can be executed."[52]

Section 148 of the Bankruptcy Act provides that upon the filing of a petition, pending foreclosure proceedings shall be stayed; however, foreclosures will not be stayed when the petitioner makes no showing of good faith.[53]

52. York v. Florida So. Corp., 310 F.2d 109 (5th Cir. 1962).

53. Mongiello Bros. Coal Corp. v. Houghtaling Properties, Inc., 309 F.2d 925 (5th Cir. 1962).